

Statement of

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BNSF



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Committee on Commerce, Science and Transportation

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My name is Stevan B. Bobb. I am Group Vice President, Agricultural Products for The Burlington Northern and Santa Fe Railway Company (“BNSF”), 2650 Lou Menk Drive, Fort Worth, Texas. I began my career in the railroad industry in 1987 with Burlington Northern and have held various positions in information systems, business analysis, and planning and yield management. In 1992, I moved to the marketing area in our company. I was appointed to my current position of Group Vice President, Agricultural Products in June 1999. I am responsible for the marketing of rail services on our system for whole grains agricultural, products, and fertilizer.

In response to the request from this Committee, I am appearing and offering this testimony for the purpose of providing information about BNSF, the role of our railroad in the movement of agricultural commodities, and the products and services we offer our customers. My testimony describes the efforts we have made over the past decade to increase the both the quality of service and the range of service products we offer our customers, as well as the role of capital investment in maintaining the infrastructure which is critical to providing that service.

I will also specifically describe our shuttle network and the efficiencies it provides our customers, as well as address aspects of our current pricing initiatives. Like other trends in the rail transportation of agricultural products over the last twenty years, the shuttle network and concept is another essential step to greater efficiency for all of us in this supply chain. Similarly, I will describe how the pricing initiatives and discounts we have made that have been the subject of concern in the last six months have been introduced to make North Dakota farmers more competitive in those markets. BNSF has responded to the market by providing rate and efficiency discounts and offering wheat customers and producers the same economic options for lower cost transportation that have been available to corn and soybean shippers, and other users of rail transportation. Thus, from a public policy standpoint, I will urge you to recognize the need for flexibility and market innovation in rail

transportation, not increased or stifling regulation, to keep us a vibrant part of the agricultural supply chain in domestic and world markets. I believe this is essential for BNSF to be able to keep making the investments in rail infrastructure necessary to allow us to provide the service North Dakota needs.

Agricultural Commodities and Products Are A Critical Part of Our Business

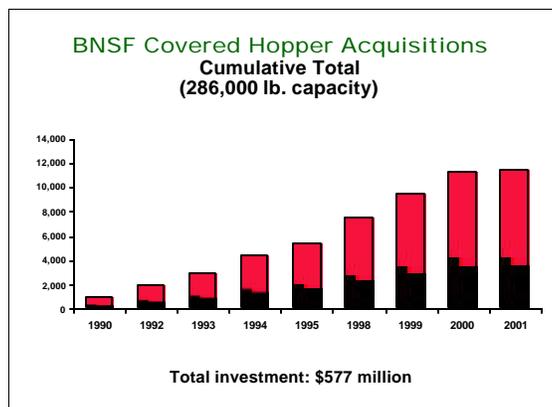
The transportation of agricultural commodities and products represented approximately 17 percent of BNSF's 2001 total freight revenues. Our business unit handles wheat, corn, sugar, high fructose corn syrup, soybeans, oil seeds and meals, feeds, barley, oats and rye, flour and mill products, milo, oils, specialty grains, malt, ethanol and fertilizer. The BNSF network is strategically located to serve the grain-producing regions of the Midwest and the Great Plains. In addition to serving most grain-producing areas, BNSF Railway serves most major domestic terminals, storage, feeding and food-processing locations. BNSF also has access to major export markets in the Pacific Northwest, the western Great Lakes, Texas Gulf and Mexico. We have historically played a key role in moving North Dakota's production to markets in the rest of the country and for export through the PNW ports.

Our railroad and our agricultural customers are a part of both a North American and a worldwide market. Our revenues from movements of agricultural products were approximately 5 percent lower in 2001 than 2000 primarily due to weaker corn export shipments to the Pacific Northwest and Mexico, and decreased shipments of Gulf and Pacific Northwest wheat, both caused by worldwide crop competition. We also saw decreased shipments of sweeteners due to an oversupply of sugar and supplier price competition in the corn syrup market, which resulted in less rail traffic of those commodities. We continually look for ways to promote the movement of agricultural commodities to and from the territories we serve, as I will discuss below.

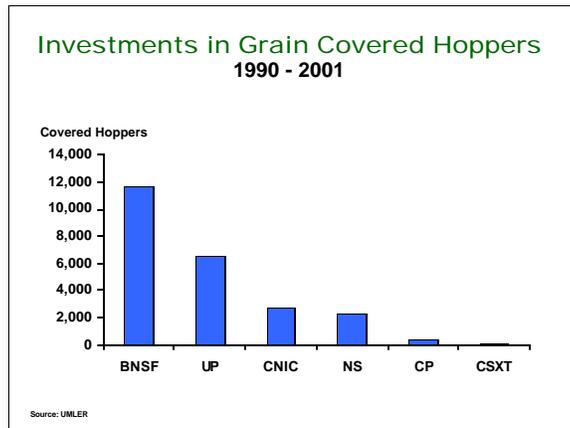
**BNSF Has Continued to Invest in Our Railroad
And Strives To Improve Our Service and Efficiency**

The key to our ability to provide our customers with the service they demand is our rail infrastructure, including equipment, track and associated structures. The BNSF merger in 1995 led to a huge capital investment program on our property. By the end of 2001, BNSF had spent about \$5.7 million per day, or \$12.5 billion, to improve our infrastructure – rails, ties, ballast, bridges, tunnels and yards; to expand our network by reopening the Stampede Pass route in Washington, by rebuilding Argentine yard in Kansas City, boosting intermodal lift capacity at hubs in Los Angeles, San Bernardino, and by building a new Stockton, California, hub, not to mention adding 500 miles of double and triple track; and acquiring some 1,700 locomotives and thousands of freight cars.

We have a fleet of almost 29,000 grain covered hopper cars, which we either acquired ourselves, by purchase or lease from car leasing companies, or lease from shippers. Over the last four years, BNSF added 5,500 heavy axle, high cubic capacity covered hopper cars. The amount of our acquisitions of covered hoppers over the last decade are shown in the chart below.



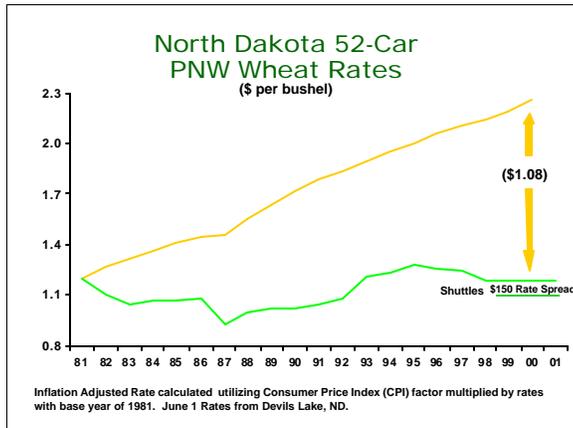
During the decade, BNSF's investment in equipment for transporting whole grains and some processed commodities has been greater than any other rail carrier.



The point of this capital investment program is that we had to spend that money in order to provide better service levels to meet our customers' expectations and to support growth, which is part of the vision of our Company.

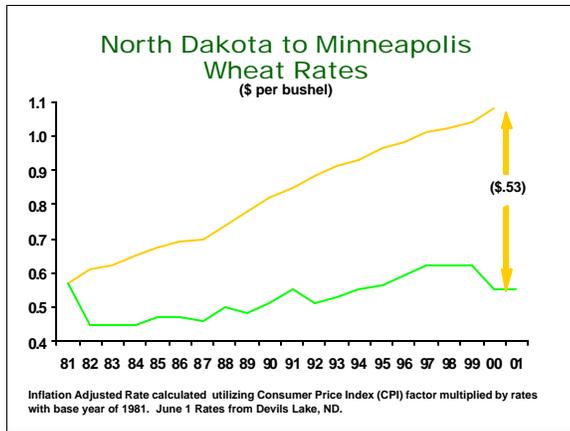
At the same time we have been making these investments, our transportation rates have been declining, and these declining rail shipping rates are benefiting both our shippers and consumers. A study released last December by the Surface Transportation Board ("Rail Rates Continue Multi-Year Decline") found that the ultimate beneficiaries of increases in rail productivity – and decreases in rail prices – have been consumers. A key finding of the study was that rail rates have fallen 45.3%, adjusted for inflation, since 1984. According to the STB, shippers would have paid an additional \$31.7 billion for rail service in 1999 if revenue per ton-mile had remained equal to the 1984 level. Another key finding was that "... all types of rail customers, and not just those with competitive transportation

alternatives, have received some portions of the rate reductions.”



This industry study reflects what

has happened at BNSF as well. Numerous examples confirm this decline. Two that stand out pertain to coal and agricultural commodities, on which I focus. BNSF’s agricultural commodities average revenue per ton-mile declined by 32%, adjusted for inflation, from 1994 through the first quarter of 2001 due to competition with both other railroads and other modes. Further, we have passed these efficiency gains through to customers in the form of lower rates in order to grow our business. The charts below compare our rates on transporting wheat to the PNW and to Minneapolis over time and the level rates would be at had we simply passed on inflation.



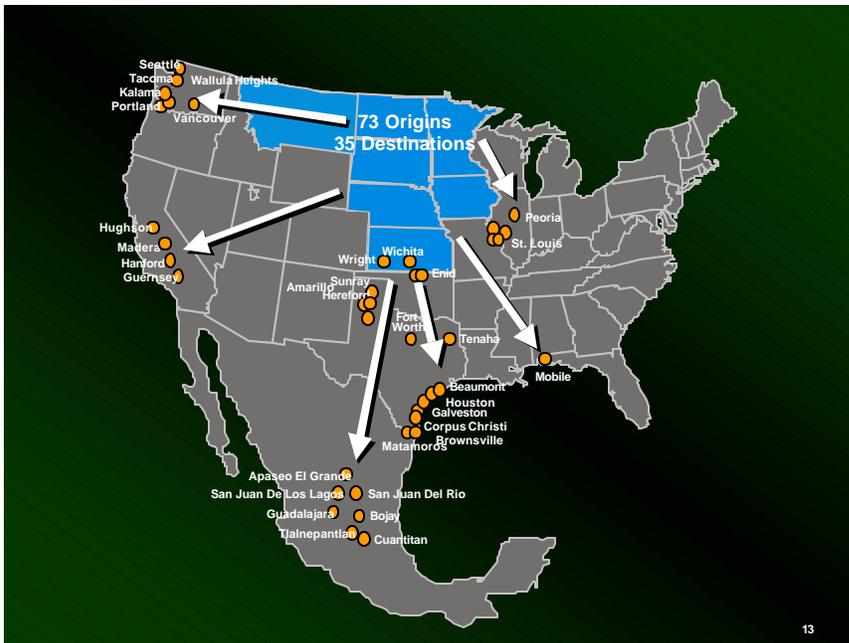
These charts reflect the same service product over the entire time period for a 52-car shipment. In each case, there has been a substantial reduction in the real cost of our services. The rates today to the PNW would be over a dollar a bushel higher, and 53 cents a bushel higher to Minneapolis, if those rates had simply reflected inflation. Additional savings have also been introduced into the market place in the form of new products, such as shuttle service, which as shown, above brings another \$150 a car reduction to the customer.

At the same time that the economic benefits of shipping on our network have improved, our service performance has improved as well. In the first quarter of this year, BNSF provided our agricultural customers with 95% on time performance for unit trains compared with 80% in 1997, and 86% in 2001. BNSF is continually sharpening its customer focus, including development of a number of e-business initiatives to make BNSF easier to do business with. We receive ongoing feedback from our customers regarding our service and that feedback during the last two years reflects both a substantial improvement as well as a positive comparison to our competition.

Infrastructure investment in the grain network has been accompanied by operational changes that have improved the efficiency and reliability of those networks. That translates into more reliable service, with fewer assets, for our grain customers. Even with these improvements, however, we understand that BNSF service is not as good as it needs to be across all commodities and across our entire network. But, it is getting better, year after year. The biggest key to further service improvements is continuously making the capital investments to increase the capacity of our network.

Because of our continuing investment in infrastructure, we have continued to improve our ability to meet customer expectations. In addition to infrastructure investment, we have also introduced new products that provide new service levels, transportation economics and capacity. Our shuttle train network, which is outlined on the map below, is a key new service offering the agricultural sector.

BNSF Grain Shuttle Network



The latest addition to our network of shuttle-loading facilities is under construction now at Ritzville, Washington. Shuttles improve utilization and velocity of grain-car assets. The shuttle network also improves utilization of locomotives and crews. Our customers gain the service benefit of using a solid train where they are not dependent on the actions of other shippers. In the case of Ritzville, we expect to grow our participation in the PNW white wheat market by being able to compete more vigorously with barges. Shuttles have also helped BNSF grow its domestic business. For example, our shuttle network has enabled us to move feedstock grain from the upper Midwest to California and to Mexico, both markets we were unable to penetrate previously.

How one views shuttles depends a lot on what one has invested in their use. Elevator operators who have not invested in shuttle-loading facilities say they do not

think shuttles are a very good idea. Their claim is that the market does not want shuttle trains. If that were the case, one could ask why then have we seen substantial customer investment in BNSF's shuttle network as well as other railroad's own versions of a shuttle program. In terms of the users of shuttles, most North Dakota shuttle loading facilities are owned by producers through local or regional co-ops, not by big grain companies. In fact, approximately 60 percent of shuttle facilities are owned by independents or local cooperatives.

The shuttle network represents the success not only of infrastructure investment by both BNSF and its customers, but also the success of taking a new approach to how we operate the infrastructure. The growth over the last five years in the shuttle network reflects the benefits our customers are reaping from this more efficient way to move grain. Grain cars in shuttle service make almost three times as many trips per month on average as the rest of the grain-car fleet, delivering the value of asset velocity and a new level of service to rail customers as well as railroads.

The grain shuttle network – the part of the grain network that works best, in terms of on-time performance and reliability – shares the characteristics of other relatively high efficiency parts of our system, such as coal and intermodal networks. Two of these characteristics are solid trains moving within a defined set of origins and destinations and well-defined service standards.

The intermodal and grain networks certainly did not start out as rationalized networks with high service standards. There were several hundred piggyback ramps, as we used to call them, handling anywhere from hundreds of units a day to just a few units a week. There were many more grain elevators years ago, many of them small ones loading only a few cars at a time.

BNSF has promoted the redesign and rationalization of both those networks

to take out the complexity inherent in trying to provide consistent, high-quality service to hundreds of locations. The process of rationalization is continuous, and it has not been done without some friction with rail shippers, elected officials and other interested parties. However, the service and efficiency benefits of rationalized, focused networks are apparent for all to see.

While the grain shuttle network provides both our customers and BNSF with the benefits of a rationalized network, BNSF continues to offer single-car, 26-car and 52-car service. The service characteristics of our grain shuttle network are very different than the service characteristics needed by many of our small shippers. While there is much rhetoric about the negative impacts of shuttles on small shippers there are no facts supporting allegations that shuttles negatively impact small shippers. The rate differential between a single-car or a 26-car shipper and a shuttle shipper is no greater than that between those smaller shipment sizes and a 52-car shipment in 1995.

Demand or Market Based Pricing Makes Sense Economically and Benefits Shippers

Most of the efficiencies we have achieved have been passed through to shippers in the form of lower prices, as STB studies have confirmed, due to competition and our need to increase volumes. Fortunately, because railroad expenses were reduced even more deeply than rates, railroads managed to keep some of the difference, which allowed the industry to gradually shore-up its finances.

We do this through “differential pricing,” which is the way virtually all industries set prices. Differential pricing, also known as demand base pricing, is the pricing of goods and services to yield various contributions to fixed costs based on the willingness and ability of various market sections to make those contributions. Costs, competitive factors, and the purchaser’s demand elasticity all get factored into the price equation. Some rail customers have argued to change

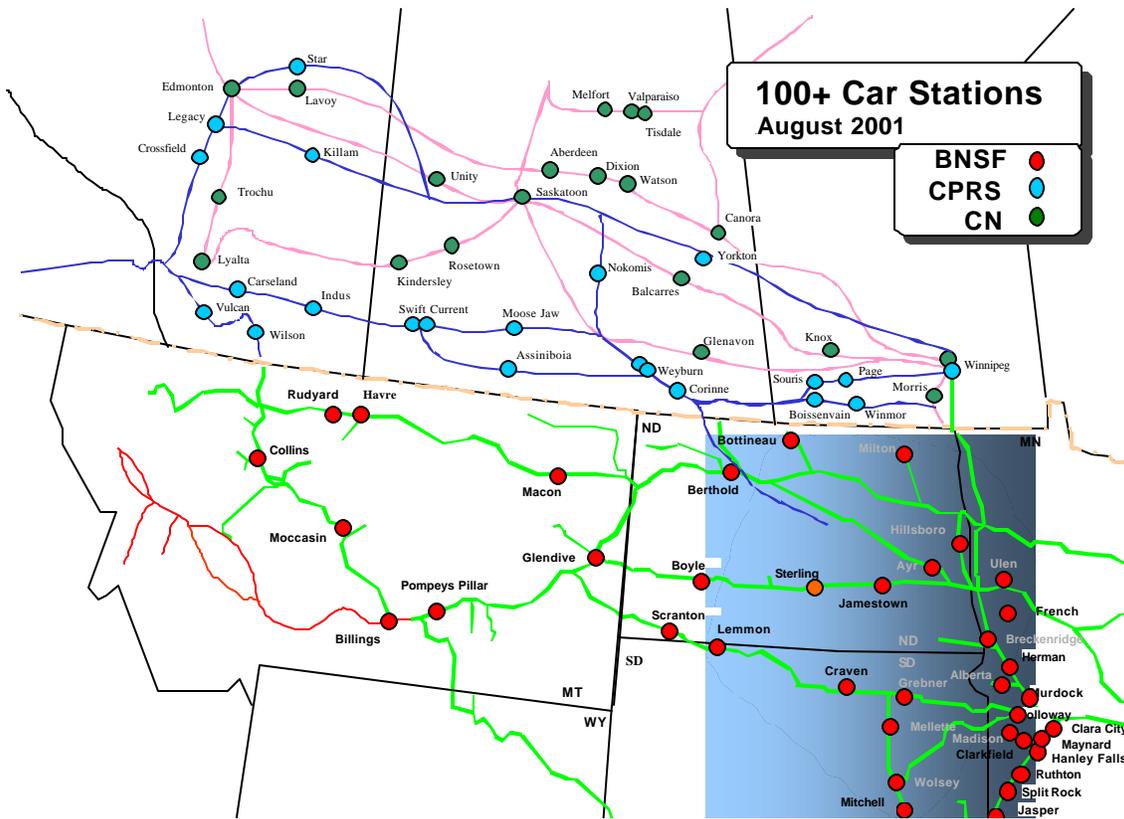
this approach to pricing, but the changes they suggest would severely and immediately constrain our ability to make capital investments. Railroads should not be denied the same pricing mechanism as other service companies.

Demand based pricing leads to different rates for movements of different commodities, for movements between different areas of the country, and on grain commodities moving to different markets. We are part of the supply chain that brings grain to markets, and we respond to that demand, as does the rest of the supply chain. What we do as a rail transportation provider is look at the difference between value of the grain at the origin and value of the grain at destination, and try to determine the level of charges for transportation with margin for the elevators to operate and make money. The fact is that winter wheat off the Texas Gulf at the destination has a lower value than hard Spring wheat off the Pacific Northwest. One can look at the value of grain at those two port destinations, and it is clear Spring wheat has a higher value. Therefore, it can stand a higher transportation cost and still move in the marketplace.

It is in our interest to move grain, not to charge rates so high that the grain cannot move. Hard Spring wheat is more valuable on a per bushel basis than winter wheat. If you look at the disappearance from the origin, there is grain disappearing from the State of North Dakota that BNSF does not handle – it goes into processors, it goes on the Canadian Pacific Railroad and it goes by truck. There are alternative markets for that grain to move to than the ones BNSF serves. If our rate does not provide a higher delivered value for the customer, the customer ships to alternative markets. We also have to compete with other sources of that grain, *i.e.*, in the case of Spring wheat out of North Dakota, we are competing with Canadian product delivered on the West Coast.

Current Differential Pricing For West Bound Export Wheat

The term that has lately also been used to describe an instance or application of market based pricing is so called "inverse pricing." I will describe how this applies in connection with our much talked about west-bound export wheat program. I believe the marketplace requires differentiated rail service. High volume rapid unload elevators at the Texas Gulf or Pacific Northwest (PNW) export terminals demand efficient high capacity train movements. Domestic flour mills and terminal markets like Duluth and Minneapolis do not yet efficiently or physically handle the larger shuttle trains. Thus, 110-car shuttle stations do not have shuttle rates to the domestic market segments which is by far the largest demand sector for eastern North Dakota wheat (see affected area shaded on the map of 100 car stations in the region below). Single, 26- and 52-car shippers must meet this demand.



Map 1

BNSF rates enable shuttle shippers to serve some select markets where shuttle efficiencies can be captured. These various alternative rate structures, like our recent PNW initiative, blend into and become a positive market factors facilitating shipments when market supply and demand for particular movements dictate. The program at issue provides just such a structure. It helps supplement, not displace, the major traditional supply sources for the PNW. It is available to take excess grain during periods of supply push (harvest) markets when traditional

terminal and mill markets are full. This program will help relieve congestion and add capacity. It continues to increase our capability to compete with trucks, and it has not diminished the value or role of our single, 26- and 52-car stations.

Table 1

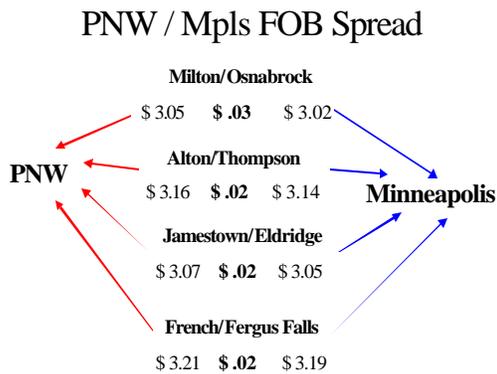
Origin	FOB Origin (Flat Price)		
	52's Basis MPLS	110's Basis PNW	Difference
Jamestown, ND		\$ 3.07	
Eldridge, ND	\$ 3.05		
Difference			\$.02
French, MN		\$ 3.21	
Fergus Falls, MN	\$ 3.19		
Difference			\$.02
Milton, ND		\$ 3.05	
Osnabrock, ND	\$ 3.02		
Difference			\$.03
Alton, ND		3.16	
Thompson, ND	\$ 3.14		
Difference			\$.02

Our efforts in this

initiative are driven by several factors. Montana's spring wheat crop is the lowest in 11 years at 65 million bushels, while spring wheat export demand from the PNW will approach 140 million bushels this year. This difference will have to be augmented from other regions. In fact, PNW export companies have indicated that the main problem that they have this year is finding enough wheat to offer to compete with Canada and Australia into the Asian market. I understand we are currently in a

demand-rationing mode, which is not healthy for the producer in the long term. Lost markets are difficult if not impossible to recover. Avoiding loss of market share to international competitors is good for Montana and North Dakota producers alike.

This initiative has also not had an adverse impact on country elevators. First, it is imperative to recognize that there is a distinction between a rate change as an absolute and the impact to the FOB value of grain at each grain facility. If a rate change is made that does not significantly change the FOB value between two elevators, there is no relative harm to the origin (single, 26 or 52-car) shipper. Our recent PNW spread initiative accomplished exactly that. While rates to the PNW have changed from North Dakota, the relative value of the grain between shippers of different unit sizes is at parity. Note the value of wheat between the 52-car market to the east and the PNW 110-car shuttle market for origins such as Eldridge and Jamestown. A market snapshot on Friday July 26, 2001, shows the FOB value quoted from both markets is only **Chart 1** 2 cents per bushel difference.



From an overall perspective, grain buying

is globally competitive. For our farmers to participate in this market, pricing has to be linked to product quality and demand. Shuttles provide farmers with

transportation efficiencies for those markets; it does not obviate the use of single car, 26 and 52-car rates.

We have also prepared a comparison of grain prices at comparable origins, for like quality, for shuttles to the PNW under our program compared with 52-car rates to the Minneapolis market (See Table 1 & Chart 1). We are told by grain companies that have bought new crop grain since our PNW program was established that the wheat was priced based on Minneapolis values and market terms. Merchandisers have included terms in their purchases which will allow them to shift or redirect the actual execution to the PNW in shuttles, if that is the best market when actual shipment takes place. These purchases are clearly not market distortive.

I believe that both for BNSF as a railroad and the consumers of our services, the development of regional elevators capable of loading large trains and our use of shuttle trains are motivated by the basic drive for efficiency as we all compete in world markets. Farmers are voting with their feet, or where they send the trucks with their grain, to obtain the benefit of these efficiencies by having their grain trucked to those regional elevators where they can obtain the best prices. Low density branch lines are costly to maintain, and are maintained with private dollars, at the same time public policy has been designed to improve the mobility of rural America by providing better roads so farmers can get their product to market. We and the elevator operators have developed a more efficient way to load, handle and transport grain using shuttle trains, and are investing in those elevators and rail assets on appropriate lines to be able to provide that service with an infrastructure that will last a long time. We will continue to serve our other elevator customers, but the most efficient will receive greater benefits, as is true across all rail systems

A Railroad Must Have the Flexibility to Adapt To the Marketplace

In the over twenty years since the passage of the Staggers Rail Act, which gave railroads more flexibility to meet market conditions, we have seen a number of positive trends in the rail transportation of agricultural products. In the late 1980's, we introduced the COTS program, which offers locked-in rates, guaranteed service, and guaranteed car supply as benefits to our customers. In the 1990's, we saw more standardization of equipment; and we increased introduction of high-capacity cars, with 286,000 lb. gross weight capacity, which are consistent, allow ease of loading, and are solely dedicated to grain customers. The shuttle network and concept is another essential step to greater efficiency for all of us in this supply chain. BNSF has responded to the market by providing North Dakota producers rate and efficiency discounts and offering wheat customers and producers the same economic options for lower cost transportation that have been available to corn and soybean shippers, and other users of rail transportation.

From a public policy standpoint, I urge you to recognize the need for flexibility and market innovation in rail transportation, not increased or stifling regulation, so we are treated on a basis consistent with what happens in other industries and can remain a vibrant part of the agricultural supply chain in domestic and world markets. This is essential for BNSF to be able to keep making the investments in rail infrastructure necessary to allow us to provide the service North Dakota needs.